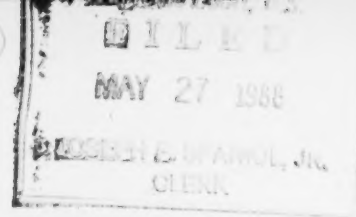


87-1962



No.

**In the
Supreme Court of the United States**

OCTOBER TERM 1987

WALTER UNTERMAYER,

Petitioner,

v.

VALHI, INC., CSX CORPORATION and
SEA-LAND CORPORATION,

Respondents.

**PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT**

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Question Presented

Section 16(b) of the Securities Exchange act of 1934 ("the 1934 Act"), 15 U.S.C. §78p(b), provides that, when a 10 percent or greater shareholder (the insider) buys and sells stock of the issuer within less than six months at a profit, that profit "shall inure to and be recoverable by the issuer"; and, if the issuer fails to sue under 16(b), any security owner may sue in its name and on its behalf.

Does a stockholder of a corporation of which the issuer subsequently became a wholly owned subsidiary, and which has failed to sue and has indemnified the insider against 16(b) liability, have standing to sue?

List of Parties

All formal parties are listed in the caption of the case in this Court.

All three respondents identified in the caption had their common stock listed on the New York Stock Exchange and registered under the 1934 Act at all relevant times, and Valhi and CSX still do. The plaintiff is a stockholder of CSX, whose wholly owned subsidiary is Sea-Land, the issuer in this case.



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Opinions Below

The opinion of the District Court for the Southern District of New York granting summary judgment to the defendants because of the plaintiff's lack of standing is reported in 665 F. Supp. 297 (S.D.N.Y. 1987) and is set out here as Appendix A.

In its first affirmance decision, the Court of Appeals did not write an opinion but made a "Summary Order" dismissing the complaint "substantially for the reasons stated" in the opinion of the District Court, with a statement (App. B, 16a): "THIS SUMMARY ORDER WILL NOT BE PUBLISHED IN THE FEDERAL REPORTER AND SHOULD NOT BE CITED OR OTHERWISE RELIED UPON IN UNRELATED CASES BEFORE THIS OR ANY OTHER COURT." The Summary Order is reported in Fed. Sec. L. Rep. (CCH), Current Vol., ¶93,607 (1988), and is set out here as Appendix B.

After the plaintiff petitioned for rehearing *en banc* (not for rehearing by the panel that had rendered the "Summary Order"), the same panel wrote an opinion, which is reported in Fed. Sec. L. Rep. (CCH) Current Vol., ¶93,690 (1988), and is set out here as Appendix C.

The plaintiff thereupon filed a second petition for rehearing *en banc*, which was denied. This order, which was filed April 13, 1988, is set out here as Appendix D.

Jurisdiction

The judgment of the Court of Appeals was entered on January 15, 1988, and affirmed on rehearing on March 7, 1988. A timely petition for rehearing *en banc* was denied on April 13, 1988. The jurisdiction of this Court is invoked under 28 U.S.C. §1254(1). The basis of the District Court's jurisdiction was §27 of the 1934 Act, 15 U.S.C. §78aa.

Statute Involved

The statutory provisions involved are §§16(a) and (b) of the 1934 Act, 15 U.S.C. §§78p(a) and (b), which relate to the recapture of certain insider short-swing trading profits. The text of these provisions is set out here in Appendix E.

Statement of the Case

The complaint alleges, and it is the fact, that Valhi, while the beneficial owner of more than 10 percent of Sea-Land common stock, bought and sold Sea-Land common stock at a profit of about \$69,000,000 within a period of less than six months.¹

¹ This states the essential facts in simplified form. Actually the purchaser was not Valhi. There were two purchasers, Amalgamated Sugar Company and LLC Corporation, both controlled by one Simmons, a notorious corporate raider. He then caused Amalgamated to merge into LLC, which was renamed Vahli. These facts are not in dispute.

(footnote continued on following page)

All parties agree that the complaint was dismissed because the plaintiff was held to have no standing, not because a 16(b) action was not adequately alleged. Therefore, the existence of a 16(b) action must be assumed *arguendo* for the purposes of this petition.

Recognizing the potentiality of 16(b) liability on the part of Valhi, CSX (which became the sole owner of Sea-Land) agreed with Valhi that it would indemnify Valhi against any 16(b) liability. Thus CSX did not sue or cause Sea-Land to sue and the plaintiff, a CSX stockholder, brought this action.

(footnote continued from following page)

The District Court's statement (App. A, 3a) that "There is no suggestion that Valhi either had access to or made unfair use of inside information" is gratuitous. For nothing is less relevant under §16(b) than whether inside information was in fact used. But we cannot let the statement stand uncorrected. For public filings with the SEC show that Valhi hired Sea-Land's former chief executive officer in order to obtain inside information.

REASONS FOR GRANTING THE WRIT

The Court of Appeals has decided an important question of federal law that has not been, but should be, settled by this Court. And it has done so in a way that (1) undermines half a century of rich jurisprudence in this Court and the Courts of Appeals that emphasizes the legislative importance of §16(b), (2) exalts form over substance, and (3) weakens a keystone weapon against insider trading at a time when evidence abounds of a repetition of the kind of practices that led to a federal scheme of regulation of the securities markets.

FIRST: Before this case, the leading case on standing in successor corporation situations was Judge Weinfeld's opinion in *Blau v. Oppenheim*, 250 F. Supp. 881 (S.D.N.Y. 1966), where the initial issuer was merged into the wholly owned subsidiary of a publicly held corporation. The plaintiff, who was suing under §16(b) to recover short-swing profits in the stock of the initial issuer, was a shareholder of the parent public corporation. He and the Securities and Exchange Commission, appearing as *amicus*, argued, as here, that the statutory term "issuer" included the subsidiary and the parent public corporation.

Judge Weinfeld denied the defendant's motion to dismiss for lack of standing, stating (*id.* at 886-87):

There is no support for the defendant's position that Congress intended that suits for the recovery of short-swing profits be restricted to the initial issuer whose securities were the subject of the illicit gains and its security holders, thus leaving no remedy in those instances where, as here, the issuer by a transfer of all its assets to another corporation has become extinct and is without

its original security holders. It is true, as defendant states, that the section makes no reference to survivor or successor corporations of an issuer—but neither does it contain any bar against the maintenance of 16(b) suits by such corporations or their security owners. To deny them the right to maintain suit would serve to defeat the purpose of the law; to accord them the right serves to further it. The defendant's position, if accepted, would substantially cut down the availability of section 16(b) as a remedy to security holders. Thus, under the defendant's concept, the right of security holders of an issuer to institute suit under section 16(b) would be terminated whenever the issuer was merged with or succeeded by another corporation; the very act of dissolution of the issuer and the failure to bring suit by the date thereof would end the right of security holders to pursue the insider and have him disgorge his profits. This hardly conforms to the essential legislative policy of section 16(b).

The defendant somewhat grudgingly concedes that his position, if upheld, would, as the SEC points out, enable unscrupulous insiders to arrange a merger or its equivalent to thwart the recovery of short-swing profits under section 16(b). (Italics supplied.)

This case was widely cited and followed by the lower courts, including the Second Circuit. *Newmark v. RKO General, Inc.*, 425 F.2d 348, 352, n. 4 (2d Cir. 1970), *cert. denied*, 400 U.S. 854. See also Judge Swygert's strong dissenting opinion in *Portnoy v. Kawecki Berylco Industries, Inc.*, 607 F.2d 765, 771 (7th Cir. 1979):

We should not expect Congress to divine—and provide for—all the possible corporate restructuring that, whether intentionally or not, can defeat

the salutary purposes of the statute. The task of accommodating a statute to a given set of facts is for the courts.

SECOND: Both lower courts here purported to distinguish *Blau* on the ground that there "the issuer had been merged out of existence," so that, "unless the issuer's successor corporation or its parent were allowed to bring a section 16(b) action, the short-swing profits illegally gained would never have been recovered," whereas "the issuer here, Sea-Land, survived the merger and remains a viable corporate entity," and "it and its shareholder, CSX, can bring an action under section 16(b)" (App. C, p. 21a-22a).

This exalts form over substance. When one company (Y) takes over another (X), the form that the transaction takes—whether (1) X merges into Y, or (2) Y buys all the stock of X, which remains in existence as a wholly owned subsidiary, or (3) X sells all its assets to Y for Y stock, which X distributes to its stockholders as a liquidating dividend—depends on many questions: the voting requirements of the particular corporation statutes, the tax consequences, the existence of franchises or labor union contracts that might or might not be assignable, and so on.

None of these factors has anything to do with the language of or the policy behind §16(b). A construction of §16(b) based solely on the distinction between a merger and a parent-subsidary situation leaves the real world. Here, just as in *Blau*, if a stockholder of the parent (CSX) is denied standing, the illicit gains would never be recovered; for this case arose out of an abortive attempt by a corporate raider to take over Sea-Land, which arranged to be acquired by CSX, a "white knight," and it was part of the deal whereby the raider left the scene that both Sea-Land and CSX waived their rights to sue under §16(b) and gave an indemnification against any §16(b) liability.

THIRD: The courts, recognizing that the stockholder is "the mere vehicle of recovery,"² have given §16(b) a particularly sympathetic reading with respect to procedural questions: the plaintiff may be a holder of *any* security, not just stock as in the ordinary derivative action; the contemporaneous stockholder requirement of F. R. Civ. P. 23.1 does not apply; the plaintiff's motive is irrelevant; intervention in company actions is freely granted "to guard against even the appearance of any concerted action."³ And standing is the quintessential gateway to the court. Surely the Congress that took such pains to guard against the issuer's being unwilling to sue one of its insiders—which is to say, by permitting *any* security holder of *any* kind to sue on the issuer's behalf—would not have foregone the case of the initial issuer's having become a *wholly owned subsidiary* of another corporation in which the plaintiff is a stockholder.

FOURTH: The decision here further entangles a pre-existing conflict among the circuits so that there is now authority for *three* rules: (1) the view here, and at least arguably in the Seventh Circuit, that a holding company stockholder may *not* sue;⁴ (2) the earlier view of the Second Circuit in *Newmark*, which followed *Blau's* holding that a stockholder of the survivor in a merger *may* sue (see p. 5 *supra*); and (3) the view of the Ninth Circuit in

² *Blau v. Lamb*, 314 F.2d 618 (2d Cir. 1963), *cert. denied*, 375 U.S. 813.

³ *Park & Tilford, Inc. v. Schulte*, 160 F.2d 984, 988 (2d Cir. 1947), *cert. denied*, 332 U.S. 761. See the collection of cases in 2 L. Loss, *Securities Regulation* 1041-42, 1046-47 (2d ed. 1961); 5 *id.* 3003-04, 3010-13 (1969 Supp.).

⁴ In *Portnoy v. Kawecki Berylco Industries, Inc.*, 607 F.2d 765 (7th Cir. 1979), *supra* p. 5, the initial issuer, whose shareholders were cashed out, became a subsidiary of a subsidiary of a public corporation, and a majority held that a stockholder of the grandparent had no standing. The Court distinguished *Blau*, as the courts here did, on the ground that in *Portnoy* the initial issuer still existed. *Id.* at 768-69.

Lewis v. McAdam, 762 F.2d 800 (9th Cir. 1985), which expressly declined to follow *Blau*, so that even a stockholder of a merger survivor may lack standing.⁵

In short, this petition presents a recurrent problem that requires the attention of this Court.

FIFTH: Hitherto this Court and the lower courts have given full rein to the legislative intention. The Senate Banking and Currency Committee stated in its 1934 report:

Among the most vicious practices unearthed at the hearings before the subcommittee was the flagrant betrayal of their fiduciary duties by directors and officers of corporations who used their positions of trust and the confidential information which came to them in such positions, to aid them in their market activities. Closely allied to this type of abuse was the unscrupulous employment of inside information by large stockholders who, while not directors and officers, exercised sufficient control over the destinies of their companies to enable them to acquire and profit by information not available to others.

Stock Exchange Practices, S. Rep. No. 1455, 73d Cong., 2d Sess. (1934) 55.

Section 16(b) was contemplated to be the answer to short-term insider trading. The peripatetic Rule 10b-5, 17 C. F. R. §240.10b-5, was not yet a dream. In any event, the contours of that rule are still indefinite, and it cannot be a substitute for the fundamentally objective §16(b). The American Law Institute so decided in its proposed Federal Securities code, concluding that §16(b) "has a symbolic significance that must be, and deserves to be, recognized." 2 ALI, *Federal Securities Code* §1714, pp. 748-52 (1980).

⁵ In *Portnoy*, *supra* p. 5, the Seventh Circuit, after distinguishing *Blau*, went on to say that in any event "*Blau* went too far in granting standing to the plaintiff" (607 F.2d at 769, n. 8).

The danger in letting the decision here stand goes beyond the question of standing in successor corporation situations. For it may encourage other wooden interpretations of §16(b). And the numerous insider trading scandals that recently have shaken public confidence in the markets make this the worst possible time for denigrating an imperfect but highly effective weapon in the securities regulatory arsenal.

CONCLUSION

The petition for a writ of certiorari should be granted.

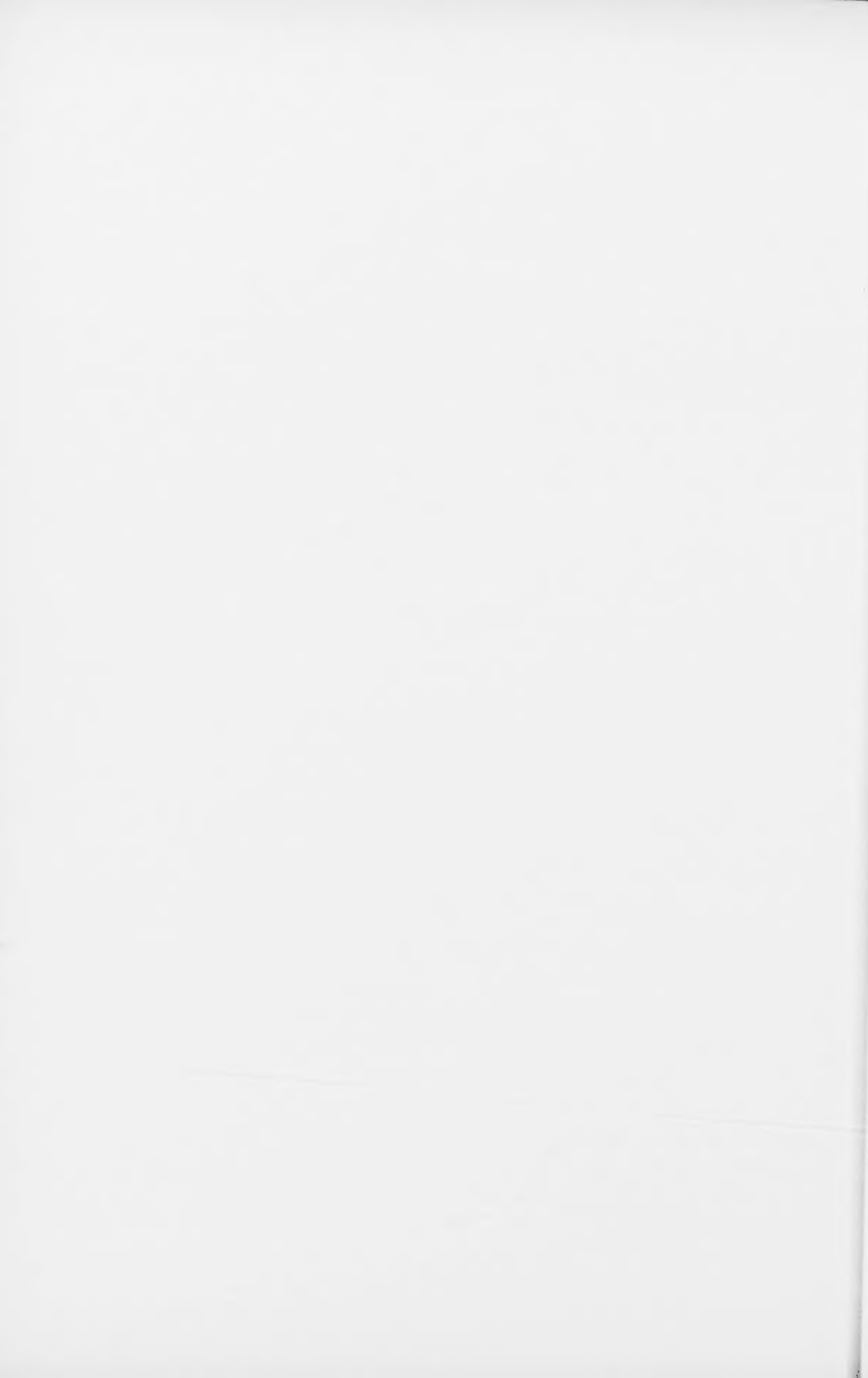
Dated: New York, New York
May 25, 1988

Respectfully submitted,

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APPENDIX A

Opinion of the District Court



UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

WALTER UNTERMEYER,

Plaintiff,

- against -

VALHI, INC., CSX CORPORATION,
and SEA-LAND CORPORATION,

Defendants.

87 Civ. 1754 (MGC)

OPINION

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CEDARBAUM, J.

Defendant Valhi, Inc. ("Valhi") moves for summary judgment pursuant to Rule 56 of the Federal Rules of Civil Procedure. The action was commenced under Section 16(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78p(b), to recover "short swing profits" realized by defendant Valhi from the purchase and sale of common stock of Sea-Land Corporation ("Sea-Land"). The motion rests on plaintiff's lack of standing. There are no contested issues of material fact which would render summary judgment inappropriate. Because I conclude that plaintiff has no standing to sue under Section 16(b), Valhi's motion is granted.

I. BACKGROUND

The verified amended complaint alleges that Valhi, while an owner of more than 10% of Sea-Land's common stock, purchased and sold Sea-Land's common stock at a profit within a period of less than six months. Valhi sold its Sea-Land stock to CSX Corporation ("CSX") for \$33.33 per share when the market price of Sea-Land's

stock was about \$28.00 per share. CSX cooperated with Valhi in attempting to disguise the sale as an option agreement, exercisable by CSX after expiration of the six-month period of Section 16(b). CSX agreed to indemnify Valhi against Section 16(b) liability, and Valhi agreed not to attempt to take over Sea-Land or CSX for ten years.

CSX acquired additional shares of Sea-Land's stock for \$28.00 per share through a cash tender offer. A subsidiary of CSX, CSX Acquisition Corp., was then merged into Sea-Land in a cash-out merger by virtue of which Sea-Land, the surviving corporation in the merger, became a wholly owned subsidiary of CSX. Plaintiff is a shareholder of CSX. CSX owns 100% of Sea-Land's common stock. Plaintiff has never owned Sea-Land stock. There is no suggestion that Valhi either had access to or made unfair use of inside information. Rather, plaintiff's claim is based solely on a violation by Valhi of the mechanical prophylactic standard of Section 16(b).

Plaintiff asserts alternative claims under Section 16(b) seeking the disgorgement of approximately \$68.8

million in short swing profits. The first claim is a "single derivative" action in behalf of CSX. The alternative claim is a "double derivative" action in behalf of Sea-Land. The amended complaint alleges futility of demand based on the agreements between Valhi and CSX. Valhi, CSX and Sea-Land are all named as defendants.

Section 16(b) provides in pertinent part that a suit may be instituted "by the issuer, or by the owner of any security of the issuer in the name and in behalf of the issuer if the issuer shall fail or refuse to bring such suit within sixty days after request...." 15 U.S.C. §78p(b). The statute defines "issuer" as "any person who issues or proposes to issue any security." 15 U.S.C. §78c(a)(8).

Valhi contends that plaintiff has no standing to bring a Section 16(b) action in behalf of CSX because CSX, as the parent of Sea-Land, is not the "issuer" within the meaning of Section 16(b), but rather is itself the owner of securities of the issuer. Valhi relies on precedent favoring a strict construction of Section 16(b) and on decisions which have declined to expand standing under that section.

With respect to the claim in behalf of Sea-Land, Valhi argues that plaintiff lacks standing because, as a shareholder of the parent of the issuer, plaintiff cannot be considered "an owner of any security of the issuer." The "double derivative" action is merely a relabeling of the same allegations. Valhi also argues that there is no justification for permitting a "double derivative" action since neither CSX nor Sea-Land was controlled by Valhi.

In opposition to Valhi's motion, plaintiff urges a construction of "issuer" that includes CSX because the violation of Section 16(b) was followed by a merger in which Sea-Land became a wholly owned subsidiary of CSX. Plaintiff argues that the remedial purpose of Section 16(b) requires such a construction because there are no minority shareholders of Sea-Land to enforce the statute. Alternatively, plaintiff argues that the standing issue is obviated because plaintiff may bring a "double derivative" suit in behalf of Sea-Land as a distinct proceeding.

II. DISCUSSION

Plaintiff's characterization of his alternative claims as "single derivative" and "double derivative" begs the question. Section 16(b) explicitly confers standing to sue, in behalf of the issuers, only on the issuer itself or on the owner of any security of the issuer. 15 U.S.C. §78p(b). Plaintiff's first claim seeks a construction of Section 16(b) that treats him as falling within the second of these two categories. He argues that "issuer" includes the parent of the issuer, and thus, as a shareholder of CSX, he is a shareholder of the issuer. In contrast, plaintiff's second claim does not purport to place plaintiff within the statutory category. Rather, he seeks to institute a "double derivative" action under Section 16(b) in behalf of Sea-Land, apparently on the theory that CSX and Sea-Land should be treated as a single entity.

No matter how plaintiff's claims are characterized, the issue raised by Valhi's motion is whether a shareholder of a corporation which owns all of the stock of an existing issuer has standing to bring a Section 16(b) suit for recovery

of short swing profits. This is a question of first impression in this Circuit. Decisions permitting multiple derivative suits in contexts not involving Section 16(b), see Goldstein v. Groesbeck, 142 F.2d 422 (2d Cir.), cert. denied, 323 U.S. 737 (1944); United States Lines, Inc. v. United States Lines Co., 96 F.2d 148, 151 (2d Cir. 1938); Fischer v. CF&I Steel Corp., 599 F. Supp. 340 (S.D.N.Y. 1984), are not applicable. It does not follow a fortiori, as plaintiff argues, that a double derivative suit is permissible under Section 16(b). The validity of multiple derivative suits in other contexts does not justify circumvention of Section 16(b)'s specific standing requirements.

Section 16(b)'s express statement of purpose is "preventing the unfair use of information which may have been obtained by [a more than 10%] beneficial owner, director, or officer by reason of his relationship to the issuer...." 15 U.S.C. §78p(b). As a means to this end, the statute provides that "any profit realized by him from any purchase and sale...of any equity security of such issuer...within any period of less than six months...shall

inure to and be recoverable by the issuer...." Id. It imposes a strict standard of liability which ordinarily is to be applied with a "mechanical quality." Reliance Electric Co. v. Emerson Electric Co., 404 U.S. 418, 425 (1972).

The Second Circuit has liberally interpreted the statute in order to effect its "broadly remedial" purpose. Adler v. Klawans, 267 F.2d 840 (2d Cir. 1959); Smolowe v. Delendo Corp., 136 F.2d 231, 239 (2d Cir.), cert. denied, 320 U.S. 751 (1943). But the statutory language may not be strained or distorted to add to the "'prophylactic' effect Congress itself clearly prescribed in §16(b)." Blau v. Lehman, 368 U.S. 403, 414 (1962). See also Reliance Electric Co. v. Emerson Electric Co., supra; Lee National Corp. v. Segur, 281 F. Supp. 851 (E.D. Pa. 1968). Holding that an "officer of the issuer" does not include an officer of a subsidiary of the issuer, the Lee court concluded:

While the purpose of the Act is to recover "short swing profits" realized by so-called "insiders," the fact is that if it be the congressional intent to include officers of subsidiary corporations as well as officers of the "issuer" corporation, this can be quickly accomplished by a single amendment to the Act. It need not be accomplished by what may be considered "judicial legislation."

281 F. Supp. at 852.

The language of Section 16(b) confers standing on an "issuer" or an "owner of any security of the issuer." 15 U.S.C. §78p(b). In support of his argument that he has standing to sue, plaintiff relies on Blau v. Oppenheim, 250 F. Supp. 881 (S.D.N.Y. 1966). In Oppenheim, the issuer was merged into the wholly owned subsidiary of a publicly held corporation in a transaction in which shares of the parent were exchanged for shares of the issuer. Thus, all shareholders of the issuer became shareholders of the parent. As a shareholder of the parent corporation, the plaintiff sued under Section 16(b) to recover short swing profits from the purchase and sale of the stock of the issuer. The court held that the parent corporation was the successor of the "issuer" and should be treated as the "issuer" for purposes of Section 16(b). In ruling that the plaintiff had standing, Judge Weinfeld looked to the remedial purpose of the statute:

[U]nder the defendant's concept, the right of security holders of an issuer to institute suit under Section 16(b) would be terminated

whenever the issuer was merged with or succeeded by another corporation; the very act of dissolution of the issuer and the failure to bring suit by the date thereof would end the right of security holders to pursue the insider and have him disgorge his profits. This hardly conforms to the essential legislative policy of Section 16(b).

250 F. Supp. at 886-87.

Oppenheim is distinguishable from the case at bar. A key fact in Oppenheim was the disappearance of the issuer and the consequent concern that no person or entity would have standing to sue under Section 16(b). 250 F. Supp. at 886. See C.R.A. Realty Corp. v. American Express, [1984 Transfer Binder] Fed. Sec. L. Rep. (CCH) §91, 528, at 98, 657 (S.D.N.Y. 1984). Here, the issuer, Sea-Land, survives as a corporate entity with CSX as its shareholder. Sea-Land itself could bring a Section 16(b) action against Valhi. If Sea-Land chose not to, CSX, as the shareholder of Sea-Land, could bring a Section 16(b) action against Valhi. If the agreements between CSX and Valhi improperly deterred CSX from bringing such an action, CSX shareholders are not without a remedy. They could bring a derivative suit against the directors and officers of

CSX for breach of fiduciary duty, a point not considered in Oppenheim.

A second significant difference is that in Oppenheim the parent corporation was in a real sense the successor of the defunct issuer. In the absence of a surviving issuer, the court construed the statutory term "issuer" to include the substantial successor of the issuer. Thus, both the parent, as "issuer," and the shareholder plaintiff, as an "owner of any security of the issuer," had standing to bring the Section 16(b) action. A justification for treating the parent as the successor issuer was that in the merger of the issuer into the parent's wholly owned subsidiary, the shareholders of the issuer received shares of the parent in exchange for their shares of the issuer. 250 F. Supp. at 883, 887. Here, however, the transaction took place without a similar exchange of securities; the parent's stock was not exchanged for stock of the issuer. Stock of the issuer was exchanged for cash. Thus, there would be no reason to consider CSX as the successor issuer of Sea-Land.

In cases not factually in point, the Second Circuit has cited Oppenheim as recognizing that the successor corporation of an issuer that no longer exists may be treated as the issuer under Section 16(b), and that, therefore, a stockholder of the successor corporation by merger has standing to sue under Section 16(b). See American Standard, Inc. v. Crane Co., 510 F.2d 1043, 1057 n.22 (2d Cir. 1974), cert. denied, 421 U.S. 1000 (1975); Newmark v. RKO General, Inc., 425 F.2d 348, 352 N.4 (2d Cir.), cert. denied, 400 U.S. 854 (1970). But the Second circuit has never held that such standing may be extended to a shareholder of the parent corporation of a surviving issuer. The language of Section 16(b) does not permit such a result.

Other circuits have refused to expand standing under Section 16(b). In Lewis v. McAdam, 762 F.2d 800 (9th Cir. 1985), the Court held that a shareholder of the parent of a wholly owned subsidiary which had absorbed the issuer did not have Section 16(b) standing. Noting that Congress is "well aware of the corporate practice of parent companies

utilizing wholly owned subsidiaries in merger transactions,"

id. at 804, the court stated:

We find nothing in the legislative history of Section 16(b) indicating that the plain meaning of the statutory language is inadequate to effect the congressional purpose of providing an enforcement mechanism against insider trading.

Id. In Portnoy v. Kawecky Berylco Industries, Inc., 607 F.2d 765 (7th Cir. 1979), upon a similar finding of legislative intent, the court refused to extend standing to a shareholder of the parent of the parent of the issuer. Id. at 767-69.

III. CONCLUSION

For the reasons discussed above, plaintiff is not authorized by Section 16(b) of the Securities Exchange Act to institute a suit in behalf of CSX or Sea-Land with respect to transactions in the common stock of Sea-Land. Accordingly, defendant Valhi's motion for summary judgment is granted.

Since this action is brought in behalf of Sea-Land and CSX, and those corporations are named as nominal defendants only, summary judgment for Valhi entirely

14a

disposes of plaintiff's claim and requires dismissal as to
Sea-Land and CSX.

SO ORDERED.

Dated: New York, New York
July 28, 1987

MIRIAM GOLDMAN CEDARBAUM
United States District Judge

APPENDIX B

First Affirmance Order of the Court of Appeals

UNITED STATES COURT OF APPEALS
FOR THE
SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 15th day of January, one thousand nine hundred and eighty-eight.

Present:

HONORABLE RICHARD J. CARDAMONE

HONORABLE GEORGE C. PRATT

HONORABLE FRANK X. ALTIMARI

Circuit Judges

WALTER UNTERMAYER,

Plaintiff-Appellant,

- against -

VALHI, INC., CSX CORPORATION and
SEA-LAND CORPORATION,

Defendants-Appellees.

ORDER
Docket No.
87-7697

Plaintiff Walter Untermeyer appeals from the July 29, 1987 judgment of the United States District Court for the Southern District of New York (Cedarbaum, J.)

pursuant to an opinion dated July 28, 1987 granting the motion of defendant Valhi, Inc. for summary judgment and dismissing plaintiff's complaint pursuant to §16(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78p.

We affirm substantially for the reasons stated in Judge Cedarbaum's thorough opinion.

Richard J. Cardamone, U.S.C.J.

George C. Pratt, U.S.C.J.

Frank X. Altimari, U.S.C.J.

N.B. THIS SUMMARY ORDER
WILL NOT BE PUBLISHED IN
THE FEDERAL REPORTER
AND SHOULD NOT BE CITED
OR OTHERWISE RELIED UPON
IN UNRELATED CASES BEFORE
THIS OR ANY OTHER COURT.

APPENDIX C

**Order of the Court of Appeals Granting
Motion for Reargument and Opinion of
Affirmance**



UNITED STATES COURT OF APPEALS
FOR THE
SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 7th day of March, one thousand nine hundred and eighty-eight.

Present:

HONORABLE RICHARD J. CARDAMONE

HONORABLE GEORGE C. PRATT

HONORABLE FRANK X. ALTIMARI

Circuit Judges

WALTER UNTERMAYER,

Plaintiff-Appellant,

- against -

No. 87-7697

VALHI, INC., CSX CORPORATION and
SEA-LAND CORPORATION,

Defendants-Appellees.

Plaintiff-appellant Walter Untermeyer having filed a petition for rehearing on January 28, 1988 which this court treats as a motion for reargument.

Upon consideration by the panel that heard the appeal, it is ordered that the motion is granted. The case is resubmitted to the panel for consideration of the arguments raised in the petition. No further submissions are required of the parties unless otherwise directed by this court, nor is any additional oral argument necessary.

Richard J. Cardamone, U.S.C.J.

George C. Pratt, U.S.C.J.

Frank X. Altimari, U.S.C.J.

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 486 - August Term, 1987

Argued: January 14, 1988 Decided: January 15, 1988

Submitted: March 7, 1988 Decided: March 7, 1988

Docket No. 87-7697

WALTER UNTERMEYER,

Plaintiff-Appellant,

- v. -

VALHI, INC., CSX CORPORATION and
SEA-LAND CORPORATION,

Defendants-Appellees.

BEFORE:

CARDAMONE, PRATT and ALTIMARI,

Circuit Judges.

Rehearing of an appeal from a judgment of the United States District Court for the Southern District of New York (Cedarbaum, Judge), granting defendant-appellee's

motion for summary judgment and dismissing plaintiff-appellant's complaint.

Affirmed.

LOUIS LOSS, Cambridge, MA (Irving Malchman, Kaufman Malchman Kaufman & Kirby, New York, N.Y., of counsel), for plaintiff-appellant.

DANIEL F. ATTRIDGE, Washington, D.C. (Jeffrey S. Davidson, John G. Froemming, Kirkland & Ellis, Washington, D.C., James K. Leader, Townley & Updike, New York, N.Y., of counsel) for defendant-appellee.

PER CURIAM:

In the prior unpublished decision of this court, Docket No. 87-7697 (2d Cir. Jan. 15, 1988), we summarily affirmed the district court's decision which granted Valhi, Inc.'s motion for summary judgment and dismissed Untermeyer's complaint brought pursuant to Section 16(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78p. On January 28, 1988, Untermeyer filed the instant petition for rehearing in which he argues that our decision affirming the district court here overrules sotto voce Blau v. Oppenheim, 250 F. Supp. 881 (S.D.N.Y. 1966). We treated Untermeyer's

petition as a motion for reargument, which was granted on March 7, 1988, and the matter was resubmitted on that date.

Having reviewed the arguments raised in Untermeyer's petition, we find none that compel a result different than that reached in our prior decision. Accordingly, we again affirm the district court's decision for substantially the reasons stated in its opinion. See 665 F. Supp. 297 (S.D.N.Y. 1987). We observe, however, that, despite Untermeyer's arguments to the contrary, the district court's decision in the instant case is not necessarily at odds with the decision in Blau v. Oppenheim. In Blau, the issuer had been merged out of existence. See Blau, 250 F. Supp. at 886. Thus, unless the issuer's successor corporation or its parent were allowed to bring a Section 16(b) action, the short swing-profits illegally gained would never have been recovered. Id. In contrast, the issuer here, Sea-Land, survived the merger and remains a viable corporate entity. See 665 F. Supp. at 298-99, 300. Because Sea-Land remains a viable corporate entity, it or its shareholder, CSX, can

bring an action under Section 16(b) to recover the short-swing profits allegedly gained. The district court in the instant case recognized this and other important distinctions, id. at 300-01, and nowhere did the district court suggest that its decision overrules Blau. Likewise, nothing in our affirmance of the district court's decision here is intended to alter the decision in Blau.

Affirmed.

APPENDIX D

**Order of Court of Appeals
Denying Petition for Rehearing**



UNITED STATES COURT OF APPEALS
FOR THE
SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 13th day of April, one thousand nine hundred and eighty-eight.

WALTER UNTERMEYER,

Plaintiff-Appellant,

- against -

No. 87-7697

VALHI, INC., CSX CORPORATION and
SEA-LAND CORPORATION,

Defendants-Appellees.

A petition for rehearing containing a suggestion that the action be reheard in banc having been filed herein by counsel for the plaintiff-appellant, Walter Untermeyer, Upon consideration by the panel that heard the appeal, it is

Ordered that said petition for rehearing is DENIED.

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges of the court

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in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereon.

Elaine B. Goldsmith,
Clerk

APPENDIX E

**Sections 16(a) and (b) of
Securities Exchange Act of 1934**



**DIRECTORS, OFFICERS, AND PRINCIPAL
STOCKHOLDERS**

Sec. 16. (a) Every person who is directly or indirectly the beneficial owner of more than 10 per centum of any class of any equity security (other than an exempted security) which is registered pursuant to Section 12 of this title, or who is director or an officer of the issuer of such security, shall file, at the time of the registration of such security on a national securities exchange or by the effective date of a registration statement filed pursuant to Section 12(g) of this title, or within ten days after he becomes such beneficial owner, director, or officer, a statement with the Commission (and, if such security is registered on a national securities exchange, also with the exchange) of the amount of all equity securities of such issuer of which he is the beneficial owner, and within ten days after the close of each calendar month thereafter, if there has been a change in such ownership during such month, shall file with the Commission (and if such security is registered on a national securities exchange, shall also file with the exchange), a statement indicating his ownership

at the close of the calendar month and such changes in his ownership as have occurred during such calendar month.

(b) For the purpose of preventing the unfair use of information which may have been obtained by such beneficial owner, director, or officer by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity security of such issuer (other than an exempted security) within any period of less than six months, unless such security was acquired in good faith in connection with a debt previously contracted, shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months. Suit to recover such profit may be instituted at law or in equity in any court of competent jurisdiction by the issuer, or by the owner of any security of the issuer in the name and in behalf of the issuer if the issuer shall fail or refuse to bring such suit

within sixty days after request or shall fail diligently to prosecute the same thereafter; but no such suit shall be brought more than two years after the date such profit was realized. This subsection shall not be construed to cover any transaction where such beneficial owner was not such both at the time of the purchase and sale, or the sale and purchase, of the security involved, or any transaction or transactions which the Commission by rules and regulations may exempt as not comprehended within the purpose of this subsection.

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No. 87-1962

Supreme Court, U.S.
FILED
JUN 27 1988

JOSEPH E. SPANIO, JR.
CLERK

IN THE
Supreme Court of the United States
OCTOBER TERM, 1987

WALTER UNTERMEYER,
v. *Petitioner,*

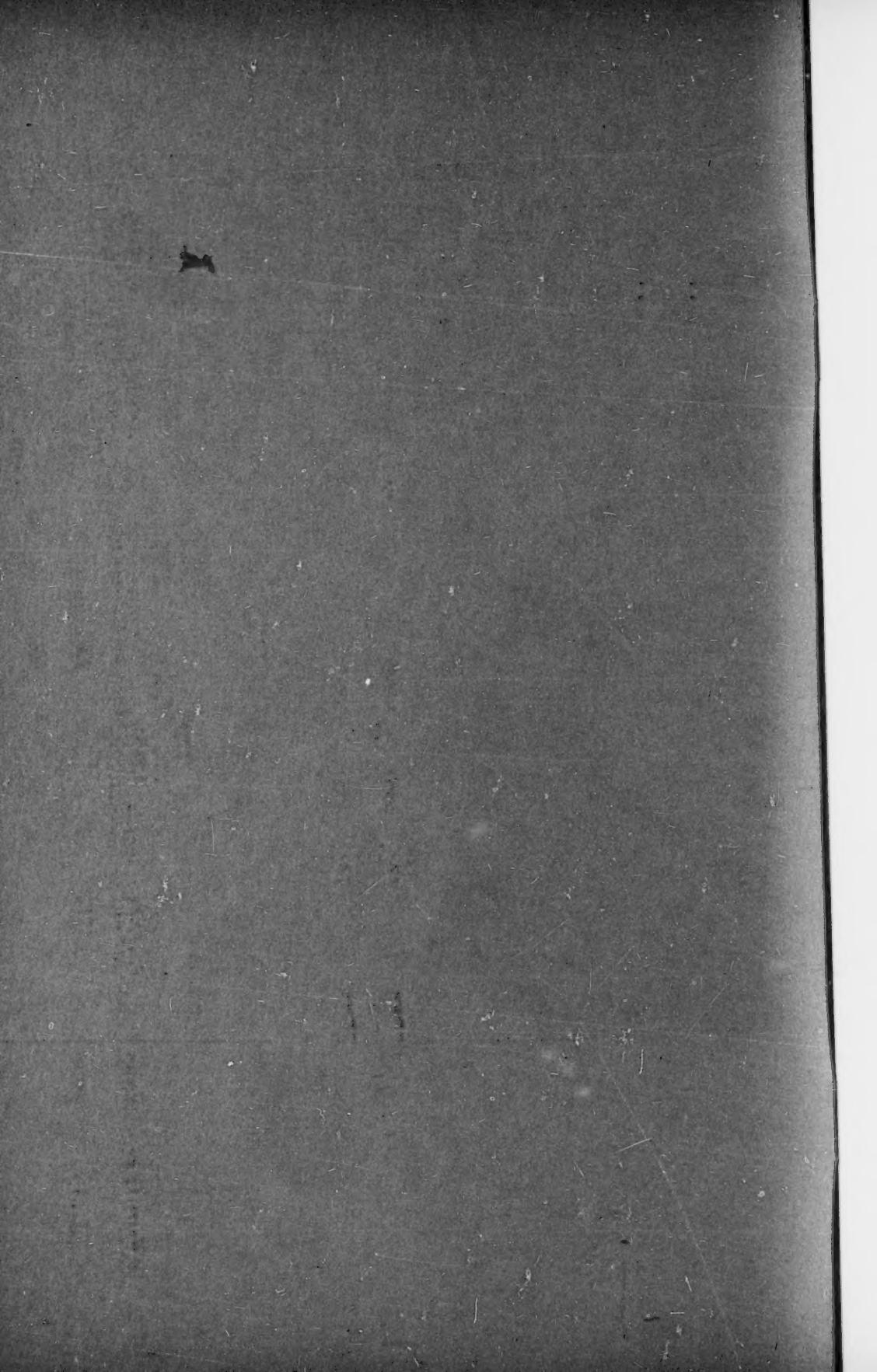
VALHI, INC., CSX CORPORATION AND
SEA-LAND CORPORATION,
Respondents.

On Petition for a Writ of Certiorari to the
United States Court of Appeals
for the Second Circuit

BRIEF FOR RESPONDENT VALHI, INC.
IN OPPOSITION

DANIEL F. ATTRIDGE
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Dated: June 27, 1988



QUESTION PRESENTED

Section 16(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78p(b), authorizes only the “issuer” or an “owner of any security of the issuer” to bring suit. The Second Circuit held that petitioner, who owns securities not of the issuer but of the parent corporation of the issuer, lacks standing to sue under section 16(b).

The Second Circuit’s holding follows the decisions of other Courts of Appeals. *Lewis v. McAdam*, 762 F.2d 800, 803-04 (9th Cir. 1985) (“shareholder of the parent corporation . . . lacks standing to bring a section 16(b) action”); *Portnoy v. Kawecki Berylco Industries, Inc.*, 607 F.2d 765, 767-69 (7th Cir. 1979) (shareholder of the issuer’s corporate grandparent cannot maintain a section 16(b) suit). The Second Circuit factually distinguished *Blau v. Oppenheim*, 250 F. Supp. 881 (S.D.N.Y. 1966), an unreviewed opinion that petitioner claims to be controlling.

Accordingly, the question presented is: whether the Second Circuit erred in following the Ninth and Seventh Circuits’ decisions in *Lewis* and *Portnoy*, respectively, and in distinguishing on its facts a 1966 opinion of a district judge in its Circuit,

STATEMENT PURSUANT TO RULE 28.1

This brief in opposition to the petition for a writ of certiorari is filed on behalf of Valhi, Inc. Valhi's corporate parents are Contran Corporation, National City Lines, Inc., and Valhi Group, Inc. Excluding wholly-owned subsidiaries, Valhi's subsidiary is NL Industries, Inc. Valhi is directly affiliated with Dixie Products, Inc. Valhi is also indirectly affiliated with the aforementioned companies' subsidiaries or affiliates, none of which is publicly traded with the exception of Keystone Consolidated Industries, Inc., Sybra, Inc., and T.I.M.E.-DC, Inc.

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IN THE
Supreme Court of the United States

OCTOBER TERM, 1987

No. 87-1962

WALTER UNTERMAYER,
v. *Petitioner,*

VALHI, INC., CSX CORPORATION AND
SEA-LAND CORPORATION,
Respondents.

On Petition for a Writ of Certiorari to the
United States Court of Appeals
for the Second Circuit

BRIEF FOR RESPONDENT VALHI, INC.
IN OPPOSITION

Untermeyer's petition for a writ of certiorari raises no issue meriting this Court's attention. The unanimous Second Circuit panel properly affirmed the District Court's holding that petitioner, a shareholder of the parent corporation of the issuer, lacks standing to bring suit under section 16(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78p(b). The decision below is entirely consistent with case law from other Circuits, *Lewis v. McAdam*, 762 F.2d 800, 803-04 (9th Cir. 1985); *Portnoy v. Kawecky Berylco Industries, Inc.*, 607 F.2d 765, 767-69 (7th Cir. 1979), as well as this Court's own securities law precedents on standing and section

16(b), and the legislative history and purpose of the statutory provision. The Second Circuit properly distinguished *Blau v. Oppenheim*, 250 F. Supp. 881 (S.D.N.Y. 1966), an uncontrolling opinion that is inapposite here. The ruling below neither conflicts with the decisions of this Court nor presents any significant federal question which calls for this Court to grant certiorari. The petition, therefore, should be denied.

COUNTER-STATEMENT OF THE CASE

The "facts" Untermeyer presents in his petition are predicated on allegations of his pleadings, not on any record evidence. Such a predicate is both improper and inadequate, for Untermeyer was confronted below with a summary judgment motion. This Court does not permit "a party opposing summary judgment to resist a properly made motion by reference only to its pleadings." *Celotex Corp. v. Catrett*, 477 U.S. 317, 325 (1986). The "plaintiff must present affirmative evidence," *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 257 (1986), but Untermeyer never did.¹

In contrast, respondent Valhi presented concrete evidence in support of its summary judgment motion. (App. 31-119.) That evidence established the following undisputed material facts:

1. Untermeyer purports to bring this suit under section 16(b) to recover certain profits allegedly received by predecessors of Valhi from trading in shares of common stock of Sea-Land Corporation. (App. 118, ¶ 1.)

¹ Thus, contrary to Untermeyer's unsubstantiated allegations, the Court cannot assume that Valhi bought and sold any Sea-Land shares within six months, that Valhi had access to any inside information, or that Valhi was improperly indemnified against any section 16(b) liability. No evidence was offered to the District Court in support of any of these claims.

2. Untermeyer allegedly is a stockholder of CSX Corporation. He has never owned any securities of Sea-Land. (App. 118, ¶ 2.)

3. After the transaction at issue, a CSX subsidiary was merged into Sea-Land. As a result, CSX became the owner of all of the shares of Sea-Land common stock. (App. 118-19, ¶ 3; 31-117.)

Based on those evidentiary facts, Valhi moved for summary judgment against Untermeyer. After briefing and argument, the motion was granted by Judge Cedarbaum in a published opinion. *Untermeyer v. Valhi, Inc.*, 665 F. Supp. 297 (S.D.N.Y. 1987). On appeal, the Second Circuit unanimously affirmed (P.B. 15a-16a) and, on Untermeyer's motion for rehearing, issued a published decision unanimously reaffirming the entry of summary judgment. *Untermeyer v. Valhi, Inc.*, 841 F.2d 25 (2d Cir. 1988). The Second Circuit rejected Untermeyer's suggestion for rehearing *en banc*. (P.B. 23a-24a.)

REASONS FOR DENYING THE PETITION

Review by this Court is "not a matter of right" but "will be granted only when there are special and important reasons therefor." Sup. Ct. R. 17.1. Petitioner does not identify any issue meriting this Court's attention. Instead, he repackages the same argument he unsuccessfully presented below. Both the District Court and the Second Circuit carefully considered petitioner's argument and rejected it as contrary to well-established federal precedent and without foundation in fact. This Court should not disturb those rulings.

I. THE UNANIMOUS SECOND CIRCUIT PANEL CORRECTLY RULED THAT PETITIONER LACKS STANDING TO BRING ANY SUIT UNDER SECTION 16(b) CONCERNING SEA-LAND SECURITIES.

Section 16(b) provides that a suit thereunder to recover for trading in an issuer's securities may be instituted only "by the issuer, or by the owner of any security

of the issuer in the name and in behalf of the issuer if the issuer shall fail or refuse to bring such suit within sixty days after request or shall fail diligently to prosecute the same thereafter.” 15 U.S.C. § 78p(b).² The term “issuer” is specifically defined to mean the “person who issues or proposes to issue any security.” 15 U.S.C. § 78c(a)(8). It is undisputed that the issuer here is Sea-Land.

Because Untermeyer has neither issued nor owned any Sea-Land securities, the District Court and the Second Circuit held that he lacked standing to sue under section 16(b). In so holding, the Courts below rejected petitioner’s request that the statutory definition of “issuer” be judicially changed to encompass not only Sea-Land but its parent corporation CSX as well. As a shareholder of the parent of the issuer—not of the issuer—Untermeyer cannot bring a section 16(b) suit.

Although he asserts that the Second Circuit’s ruling “undermines half a century of rich jurisprudence in this Court and the Courts of Appeals” (P.B. 4), Untermeyer does not cite a single Supreme Court case in his petition. Nor does he identify a single case from any Court of Appeals applying the statutory definition of “issuer” in the way he proposes. All of this is unsurprising, since petitioner’s approach is contrary to directly applicable federal decisions applying the statutory definition, is inconsistent with this Court’s securities law precedents, and is unsupported by section 16(b)’s legislative history and purpose.

A. The Decision Below Follows Well-Settled, Directly Applicable Federal Precedents.

The Second Circuit’s holding follows all the directly applicable decisions from other Circuits. The Ninth and Seventh Circuits, as well as a District Court in the Third

² All emphasis added unless otherwise indicated.

Circuit, have all rejected attempts to broaden the meaning of the term "issuer" beyond its statutory definition. The cases consistently hold that one must be a shareholder of the "issuer"—not merely of its corporate parent, grandparent or subsidiary—to have standing to sue under section 16(b).

In *Lewis v. McAdam*, 762 F.2d 800 (9th Cir. 1985), the key issue was precisely the same one addressed below: whether "a shareholder of the parent may be deemed an 'owner of a security in the issuer' for purposes of bringing a section 16(b) action." *Id.* at 803. After analyzing the text and legislative history of section 16(b), the Ninth Circuit concluded that Congress did not intend to permit a shareholder of the issuer's parent to bring suit:

We find nothing in the legislative history of section 16(b) indicating that the plain meaning of the statutory language is inadequate to effect the congressional purpose of providing an enforcement mechanism against insider trading. That a merger may result in a corporation succeeding to an action formerly held by an individual is a consequence dictated by the statute. We will not confer standing on a plaintiff who falls outside the class of persons permitted by the language of the statute to bring suit merely because the only parties falling within the class choose not to exercise their right to sue.

Congress is well aware of the corporate practice of parent companies utilizing wholly owned subsidiaries in merger transactions. Had Congress wanted to discourage this practice by conferring standing on shareholders of a parent corporation whose wholly owned subsidiary absorbed the original issuing corporation, it knew how to do so. Accordingly, *we conclude that Congress included in the statutory language of section 16(b) all the remedies it deemed appropriate.*

Id. at 804 (citations omitted). Thus, the Ninth Circuit held:

[T]he parent corporation is not an "issuer" within the meaning of section 16(b). Similarly, *a shareholder of the parent corporation cannot be considered an "owner of any security of the issuer" and accordingly lacks standing to bring a section 16(b) action.* In the case before us, Sears is not a section 16(b) "issuer," and Lewis, who owned stock in neither SDC nor Coldwell Banker, lacks standing under the statute.

Id.

In *Portnoy v. Kawecky Berylco Industries, Inc.*, 607 F.2d 765 (7th Cir. 1979), the critical issue was whether the plaintiff's status as a shareholder of Cabot (the parent of the parent of the issuer) gave him standing to sue under section 16(b). Based on a thorough analysis of the pertinent statutory provisions and case law, the Seventh Circuit refused to draft "judicial legislation" to grant the plaintiff standing:

The statutory language is thus specific that the issuer is the person who issues the security which is involved in the short-swing trading, in this case, KBI.

The plaintiff asks us to broaden the definition to encompass Cabot which would make the issuer include the parent of the parent of the issuer. . . . [W]e cannot rewrite the statute to accommodate this situation. Congress has spoken clearly. When it wanted a broader definition of issuer, it drafted one. In § 2(a)(11) of the Securities Act of 1933, for example, "issuer" is defined as including "any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer." 15 U.S.C. § 77b(11). In § 16(b), on the other hand, *Congress apparently intended only those with a less tenuous financial interest to have standing and confined standing other than to the "issuer" itself to "the owner of any security of the issuer."*

. . . We similarly reject the plaintiff's invitation to draft "judicial legislation to grant him standing."

Id. at 767-68 (footnotes omitted). Because Portnoy was not a shareholder of the issuer, the Seventh Circuit held that he lacked standing to sue.

Lee National Corp. v. Segur, 281 F. Supp. 851 (E.D. Pa. 1968), while technically not a standing case, turned on whether the statutory definition of "issuer" included a corporation's wholly-owned subsidiary. Judge Troutman held that an officer of a wholly-owned subsidiary is not an officer of the "issuer" within the meaning of section 16(b):

[Plaintiff's counsel] seeks a judicial broadening of the specific and express language of the statute. . . . [T]he fact is that if it be the congressional intent to include officers of subsidiary corporations as well as officers of the "issuer" corporation, this can be quickly accomplished by a single amendment to the Act. It need not be accomplished by what may be considered "judicial legislation."

Id. at 852. Accordingly, the complaint there was dismissed as it sought "a broad interpretation of the statute not warranted and justified by the language of the statute. *Id.*³

The Second Circuit's decision below is also consistent with *American Standard, Inc. v. Crane Co.*, 510 F.2d 1043 (2d Cir. 1974), *cert. denied*, 421 U.S. 1000 (1975). There the Second Circuit ruled that "issuer" cannot be construed to encompass multiple entities, rather than just the single issuing corporation:

³ The result in *Lee National* was endorsed by the Seventh Circuit in *Portnoy*, 607 F.2d at 768, as well as by the SEC. See Interpretive Release on Rules Applicable to Insider Reporting and Trading, Exchange Act Release No. 18,114, 23 SEC Docket 856, 861 (Sept. 23, 1981) (president of a wholly-owned subsidiary "would not ordinarily be considered an officer under Section 16(a) since he is not an officer of the issuer").

The statute speaks of "such issuer" in the singular. There is no room for a grammatical construction that would convert the singular into a plural. Nor does the internal construction of the section lend itself to such a free interpretation.

....

... The style and substance lead to the conclusion that Congress was concerned with a single issuer.

Id. at 1058-59 (holding that the purchase of shares of one issuer cannot be matched against the sale of shares of a successor issuer).

In short, the decision below raises no conflict with the well-established, uncontroverted case law from other Circuits. The results reached by the Ninth Circuit in *Lewis*, the Seventh Circuit in *Portnoy*, the Third Circuit District Court in *Lee National*, and the Second Circuit in *Untermeyer* below are all in accord and are all correct.

B. The Decision Below Is Fully Consistent With This Court's Guiding Securities Law Precedents.

Untermeyer's petition makes no mention of any of this Court's securities law precedents. This is no wonder given that these precedents support the decision below and contradict the approach he advocates.

This Court has strictly construed the standing requirements of the Securities Exchange Act. See *Piper v. Chris-Craft Industries, Inc.*, 430 U.S. 1, 24-46 (1977) (tender offeror lacks standing to sue for damages under section 14(e), 15 U.S.C. § 78n(e), or SEC Rule 10b-5, 17 C.F.R. § 240.10b-5); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 731-55 (1975) (only actual purchasers and sellers have standing to sue for damages under SEC Rule 10b-5). This restrictive approach avoids the "danger of vexatious litigation which could result from a widely expanded class of plaintiffs." 421 U.S. at 740, *quoted in*

Santa Fe Industries, Inc. v. Green, 430 U.S. 462, 479 (1977).⁴

Specifically, this Court has refused to impose liability under section 16(b) where it would involve a departure from the statutory language. In *Reliance Electric Co. v. Emerson Electric Co.*, 404 U.S. 418 (1972), this Court held that a statutory insider, a "beneficial owner of more than 10 per centum," may properly "sell enough shares to bring his holdings below 10%, and later—but still within six months—sell additional shares free from liability under the statute." *Id.* at 423. The language used by Congress in section 16(b) to limit liability must be "[r]ead literally" and applied with a "mechanical quality." *Id.* at 423, 425. Courts "are not free to adopt a construction that not only strains, but flatly contradicts, the words of the statute." *Id.* at 427.

Similarly, in *Foremost-McKesson, Inc. v. Provident Securities Co.*, 423 U.S. 232, 239-60 (1976), this Court held that section 16(b) does not apply to a "beneficial owner of more than 10 per centum" of the issuer's securities unless his holdings are above 10% at the time of both his purchase and sale of securities. Section 16(b) has "narrowly drawn limits." *Id.* at 251. Liability must not be imposed unless Congress' statutory language authorizes it "expressly or by unmistakable inference." *Id.* at 252.

And in *Blau v. Lehman*, 368 U.S. 403, 409-14 (1962), this Court held that a Lehman Brothers partner sitting on a company's board of directors was not a "director" deputized by Lehman so as to make the partnership liable for profits it "realized" from short-swing trading in the

⁴ This Court is well aware that "even a complaint which by objective standards may have very little chance of success at trial has a settlement value to the plaintiff out of any proportion to its prospect of success at trial so long as he may prevent the suit from being resolved against him by dismissal or summary judgment." *Blue Chip Stamps*, 421 U.S. at 740.

company's stock. In so holding, the Court rejected the SEC's invitation to rewrite section 16(b)'s terms to the extent liability was "*not justified by the literal language of § 16(b).*" *Id.* at 411. "Congress is the proper agency to change an interpretation of the Act unbroken since its passage, if the change is to be made." *Id.* at 413. Liability cannot be extended "by adding to the 'prophylactic' effect Congress itself clearly prescribed in § 16(b)." *Id.* at 414.

The decision below is consistent with this Court's guiding securities law precedents. The Second Circuit correctly declined to enlarge the scope of section 16(b) beyond its statutory limitations. Reading the statutory provision literally and non-expansively, a shareholder of the parent of the issuer lacks standing to sue.

C. The Decision Below Is Supported By The Legislative History And Purpose Of Section 16(b).

The legislative history of section 16(b) is devoid of any suggestion that Congress intended a shareholder of the parent of the issuer to have standing to sue. As the Ninth Circuit concluded, there is "nothing in the legislative history of section 16(b) indicating that the plain meaning of the statutory language is inadequate to effect the congressional purpose of providing an enforcement mechanism against insider trading." *Lewis*, 762 F.2d at 804. Similarly, the Second Circuit has determined: "In the legislative history we have observed no omission by inadvertence." *American Standard*, 510 F.2d at 1061.

Rather, the legislative history indicates that Congress intended recovery of short-swing profits be limited to the issuer, not extended to its corporate affiliates or their stockholders. *See* H.R. Conf. Rep. No. 1838, 73d Cong., 2d Sess. 35-36 (1934) (provision requires that profits be yielded "to the issuer"; "authorizes the issuer to recover such profit by suit"); S. Rep. No. 792, 73d Cong., 2d

Sess. 20-21 (1934) (provision makes profits "available to the issuer").

The legislative history also demonstrates that Congress intended section 16(b) to be merely "prophylactic" and did not intend to address each and every situation involving alleged short-swing trading. The House Report expressly recognized that section 16's "requirements are not air-tight" and that one "may still, within the law, use inside information for his own advantage." H.R. Rep. No. 1383, 73d Cong., 2d Sess. 13 (1934). Thus, as the District Court below stressed, the "statutory language may not be strained or distorted to add to the "prophylactic" effect Congress itself clearly prescribed in § 16(b).'" 665 F. Supp. at 300 (quoting *Blau v. Lehman*, 368 U.S. at 414).⁵

In light of this legislative history, the reach of section 16(b) must not be expanded beyond the specific statutory language. *Lewis*, 762 F.2d at 804 ("Congress included in the statutory language of section 16(b) all the remedies it deemed appropriate"); *Lee National*, 281 F. Supp. at 852 ("Courts may not give content to an Act beyond its language").

Nor would a grant of standing to petitioner serve the legislative purpose of section 16(b). That section

⁵ The gaps in section 16(b)'s coverage are many and obvious. For example, Congress limited the provision's coverage to transactions occurring within a six-month period. A statutory insider who waits six months and one day after the purchase to avoid a short-term gain is unaffected by the provision. *Adler v. Klawans*, 267 F.2d 840, 845 (2d Cir. 1959). "One can speculate on whether the moral or ethical values are altered by the passage of 24 hours but the statute makes an honest if not honorable man out of the insider in that period." *Id.* In addition, section 16(b) applies only to transactions of the issuer's directors or officers or of shareholders who own more than 10% of its equity securities. It does not affect the trading practices of 9.9% shareholders. *Foremost-McKesson*, 423 U.S. at 239-60; *Reliance Electric*, 404 U.S. at 422-27. Nor does it ordinarily affect the transactions of directors and officers of the issuer's wholly-owned subsidiary. *Lee National*, 281 F. Supp. at 852.

was designed to prevent a corporate director or officer or "the beneficial owner of more than 10 per centum" of a corporation from profiteering through short-swing securities transactions on the basis of inside information. It provides that a corporation may capture for itself the profits realized on a purchase and sale, or sale and purchase, of its securities within six months by a director, officer, or beneficial owner.

Foremost-McKesson, 423 U.S. at 234 (footnotes omitted).

The factual circumstances of this case are markedly removed from this congressional purpose. The transaction at issue did not involve a purchase and sale of a statutory insider's stock. To the contrary, petitioner seeks to challenge the grant of an option to sell Sea-Land securities to CSX. (App. 17, ¶ 13.) "But the mere execution of an option to sell is not generally regarded as a 'sale'" within the ambit of section 16(b). *Kern County Land Co. v. Occidental Petroleum Corp.*, 411 U.S. 582, 601 (1973).

Similarly, this case does not fit within the "congressional purpose of curbing short-swing speculation by corporate insiders." *Reliance Electric*, 404 U.S. at 424. Respondent Valhi is the classic outsider: an unsuccessful offeror whose bid to acquire Sea-Land was hostilely rebuffed, a position "*sui generis* in terms of § 16(b) liability." *American Standard*, 510 F.2d at 1053. While "Congress thought that all short-swing trading by directors and officers was vulnerable to abuse," it viewed trading by mere stockholders as abusive only where it "afforded the potential for access to corporate information." *Foremost-McKesson*, 423 U.S. at 253. There was no suggestion below that "Valhi either had access to or made unfair use of inside information." 665 F. Supp. at 298. And such access cannot be presumed: "the status of a defeated tender offeror affords no presumption of abuse of confidential information by virtue of relationship to the issuer." *American Standard*, 510 F.2d at 1053.

Finally, the aim of the petitioner's suit is not to restore alleged short-swing profits to the issuer Sea-Land, but to provide a gigantic bonanza to his own corporation CSX. This is a misuse of section 16(b). There is nothing but "sheer windfall" in handing a recovery to CSX, a corporation that was not in any relationship with Valhi other than as a competing bidder for Sea-Land. See *American Standard*, 510 F.2d at 1061. No such recovery may be properly allowed.

II. IN FACTUALLY DISTINGUISHING AN UNREVIEWED 1966 DECISION OF ITS DISTRICT COURT, THE SECOND CIRCUIT RAISED NO IMPORTANT QUESTION OF FEDERAL LAW REQUIRING THE ATTENTION OF THIS COURT.

Petitioner cannot demonstrate that the Second Circuit raised an important question of federal law by distinguishing *Blau v. Oppenheim*, 250 F. Supp. 881 (S.D.N.Y. 1966), on its facts. Both Courts below properly distinguished that unreviewed 1966 district court opinion in accordance with well-settled lines of federal law.

In *Blau v. Oppenheim*, a shareholder of American Can Company brought a section 16(b) suit concerning trading in the securities of Hanson-Van Winkle Mining Company. After the alleged short-swing trading, Hanson-Van Winkle sold and transferred all its assets and choses in action to M & T Chemicals, Inc., a wholly-owned subsidiary of American, and in return the Hanson-Van Winkle shareholders received shares of American stock. Hanson-Van Winkle was merged into M & T and ceased to exist. Blau was allowed to maintain the action as a shareholder of American.

As the District Court below held, the facts in *Blau v. Oppenheim* are readily distinguishable:

A key fact in *Oppenheim* was the disappearance of the issuer and the consequent concern that no person or entity would have standing to sue under section

16(b). 250 F. Supp. at 886. . . . Here, the issuer, Sea-Land, survives as a corporate entity with CSX as its shareholder. Sea-Land itself could bring a section 16(b) action against Valhi. If Sea-Land chose not to, CSX, as the shareholder of Sea-Land, could bring a section 16(b) action against Valhi. If the agreements between CSX and Valhi improperly deterred CSX from bringing such an action, CSX shareholders are not without a remedy. They could bring a derivative suit against the directors and officers of CSX for breach of fiduciary duty, a point not considered in *Oppenheim*.

A second significant difference is that in *Oppenheim* the parent corporation was in a real sense the successor of the defunct issuer. In the absence of a surviving issuer, the court construed the statutory term "issuer" to include the substantial successor of the issuer. Thus, both the parent, as "issuer," and the shareholder plaintiff, as an "owner of any security of the issuer," had standing to bring the section 16(b) action. A justification for treating the parent as the successor issuer was that in the merger of the issuer into the parent's wholly owned subsidiary, the shareholders of the issuer received shares of the parent in exchange for their shares of the issuer. 250 F. Supp. at 883, 887. Here, however, the transaction took place without a similar exchange of securities; the parent's stock was not exchanged for stock of the issuer. Stock of the issuer was exchanged for cash. Thus, there would be no reason to consider CSX as the successor issuer of Sea-Land.

665 F. Supp. at 300-01.

Affirming the District Court, the Second Circuit held that these were "important distinctions" that distinguished *Blau v. Oppenheim* from this case. 841 F.2d at 25. Notably, the Seventh Circuit in *Portnoy* also ruled the case distinguishable on essentially the same grounds:

Blau is factually distinguishable in that the issuer no longer existed, whereas in the present case KBI

still exists as a viable corporate entity. This distinction justifies the different result in *Blau*, because if the statutory language were applied to allow only shareholders of the issuer to enforce the violation, and the issuer were dissolved, the statutory language would require the absurd result that no party would exist who had standing to enforce the violation. In the present case, since KBI still exists, its shareholder, CSMC, had the right to bring the action regardless of whether it chose to exercise that right.

607 F.2d at 768-69 (footnotes omitted).⁶

In an effort to avoid these important factual distinctions, petitioner claims that *Blau v. Oppenheim* has been "followed by the lower courts, including the Second Circuit." (P.B. 5.) But what Untermeyer fails to point out is that the case has been followed only for the unremarkable proposition—not relevant here—that the suc-

⁶ *Blau v. Oppenheim* is distinguishable on other grounds as well. That case involved a "sale" of the defendant insider's stock, a transaction expressly covered by section 16(b). In contrast, Untermeyer wants to attack the grant of an "option" to sell Sea-Land securities to CSX—a transaction generally regarded as outside the reach of section 16(b). See *Kern County*, 411 U.S. at 601. Also, defendant Oppenheim, a director and officer of Hanson-Van Winkle, was a true insider. Valhi is the classic outsider, an unsuccessful offeror who neither "had access to [n]or made unfair use of inside information." 665 F. Supp. at 298. As such, no liability may sensibly be imposed on Valhi here.

Blau v. Oppenheim was also premised on an incorrect interpretation of section 16(b). The court there acknowledged that "upon a strict or literal reading of section 16(b) plaintiff never was 'the owner of any security of the issuer,'" but declined to read the statute in that manner. 250 F. Supp. at 884. This was a mistake. Under this Court's precedents, the statutory language used to limit liability must be "[r]ead literally" and non-expansively. *Reliance Electric*, 404 U.S. at 423; see *Foremost-McKesson*, 423 U.S. at 251-52 (section 16(b) has "narrowly drawn limits"; no liability can be imposed unless statutorily authorized "expressly or by unmistakable inference"); *Blau v. Lehman*, 368 U.S. at 411 (rejecting liability "not justified by the literal language of § 16(b)").

cessor corporation of a defunct issuer inherits the latter's choses in action. *American Standard*, 510 F.2d at 1057 n.22; *Newmark v. RKO General, Inc.*, 425 F.2d 348, 352 n.4 (2d Cir.), *cert. denied*, 400 U.S. 854 (1970). As the District Court below concluded, "the Second Circuit has never held that such standing may be extended to a shareholder of the parent corporation of a surviving issuer. The language of section 16(b) does not permit such a result." 665 F. Supp. at 301.

From the false premise that *Blau v. Oppenheim* has been "followed," petitioner asserts that the decision below "further entangles a preexisting conflict among the circuits." (P.B. 7.) In fact, however, there is no conflict at all. The cases cited by petitioner uniformly support two consistent legal principles: (1) a shareholder of the corporate parent (or grandparent) of the issuer lacks standing to sue under section 16(b), *Untermeyer*, 841 F.2d at 25; *Lewis*, 762 F.2d at 803-04; *Portnoy*, 607 F.2d at 767-69; and (2) where a successor corporation inherits a defunct issuer's choses in action, a shareholder of the successor has standing to sue, *Lewis*, 762 F.2d at 802-03; *Newmark*, 425 F.2d at 352 n.4.

In sum, the Courts below correctly distinguished *Blau v. Oppenheim*. And in all events, the Second Circuit's decision to distinguish rather than to overrule that case raises no issue warranting this Court's attention.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted,

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